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ABSTRACT

The availability of general liability insurance policies is addressed to help trustees assess the adequacy of protection provided by state or institutional indemnification provisions, or through one of the insurance policies currently available. The board of trustees' responsibility to monitor regularly the policy it may have in force or that it may select is also considered. Trustee liability insurance typically will pay on behalf of the trustee sums that the trustee becomes legally obligated to pay as a result of errors or omissions in the performance of duties. Five insurance companies that offer insurance for trustees and officers are identified. The bases of costs of trustee liability policies are specified, and two forms of umbrella coverage are noted. The technical aspects of indemnification clauses and actual policies are examined, including terms such as severability, discovery of facts that could give rise to a claim, exclusions, the insuring agreement, and costs and expenses of defense. Even though state indemnification statutes exist, there is lack of uniformity among the states as to the protection accorded. Ten questions that trustees can ask to acquaint themselves with the protection available in their own jurisdictions are presented. Potential problems for the insured that could arise as the policy application is being completed are discussed, and a list of risks covered by general liability insurance or trustee liability insurance is presented. A brief bibliography is included. (SW)

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Trustee Liability Insurance

A Final Report of the Association of Governing Board's Ad Hoc Committee

HE 015 060

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Introduction

The past ten years have brought a serious new concern among college and university trustees: exposure to personal and institutional lawsuits, resulting in a need for adequate liability insurance. Trustees can no longer take comfort in the proposition that if they exercise ordinary and reasonable care in the performance of their duties, exhibiting honesty and good faith, they can avoid lawsuits and the risk of personal liability. Instead, they must contend with the ever growing possibility that the discharge of their responsibilities may be subjected to legal challenge. Among the more common challenges are claims involving faculty appointment and dismissal, discrimination, investment of endowment, misuse of financial aid funds, breach of loyalty, student admissions and dismissal, conflict of interest and bankruptcy. (A more complete list, including areas that are covered by general liability policies, can be found at the end of this paper.)

The AGB Ad Hoc Committee on Trustee Liability Insurance was formed in 1980 to respond to numerous requests from member trustees for information which would help them to select an insurance policy that would best meet their particular needs and concerns.

The Committee was comprised of eight members, primarily from the legal and insurance professions:

David M. Lascell, Esquire, Chairman. Partner, Nixon, Hargrave, Devans and Doyle; Chairman, Board of Trustees, Wells College (New York); Member, AGB Board of Directors.

John F. Adams. Director, Center for Insurance Research, Georgia State University.

Ellen Diehlmann, Esquire. Vice President, Johnson and Higgins, New York.

Phillip M. Grier, Esquire. Executive Director, National Association of College and University Attorneys.

Robert L. Lewis, Esquire. Partner, Ulmer, Berne, Laronge, Glickman and Curtis; Trustee, Lake Erie College (Ohio); Trustee, Cleveland Commission on Higher Education; Member, AGB Board of Directors.

James M. Mitchell. Trustee, George Washington University (D.C.); Former Treasurer and Honorary Member, AGB Board of Directors.

Judith L. Robinson, CPCU. Vice President, H & R Phillips Inc., New York.

Edward G. Wilson, Esquire. Trustee Emeritus, Earlham College (Indiana); Former Secretary and Honorary Member, AGB Board of Directors.

The Committee, in this report, does not intend to convince chief executives and trustees that they should buy additional insurance coverage to supplement their institutions' existing general liability policy. Rather, its primary purpose is to inform trustees of the availability of such coverage and to help them assess the adequacy of protection provided by state or institutional indemnification provisions, or through one of the various insurance policies currently available.

The Committee also aims to inform interested readers that many exposures to liability usually are not covered under general liability policies and that trustees may need a separate policy of insurance directed at the specific risks which they face.

Finally, the Committee stresses the board's responsibility to monitor regularly the policy it may have in force, or that which it may ultimately select. The paper addresses these questions:

- Is there anything available to protect trustees from the risks that accompany their positions?
- Is there an insurance liability policy written expressly for boards of trustees of particular types of higher education organizations? If not, what aspects of available policies should trustees examine to ensure that they choose the one that best meets their needs?
- What questions should trustees ask—particularly those who serve public institutions—regarding their states' indemnification statutes and protection?

The AGB Board of Directors is extremely grateful to the members of the Committee, and to Linda Einstein Henderson of the AGB staff, for their contribution in shedding light on a complex and ambiguous set of issues. And they join with the Committee in reminding readers that this paper is not intended to supplant the counsel of competent legal and insurance experts.

SECTION I: Overview

Like most business organizations, many colleges and universities purchase general liability insurance to provide protection for the negligent acts of their employees, e.g., the faulty step on which a visitor falls. In recent years, however, an increasing number of institutions also have sought supplemental insurance specifically for members of their governing boards.

A not-for-profit or charitable organization, such as a college or university, has the authority—and the responsibility—to protect its regents, trustees or governors if they are sued. The cost of even a spurious suit can be significant for all but the wealthiest institutions. Lawyers' fees, staff time and related expenses mount quickly, even if it is determined finally that the actions of the governing board members do not justify any award at all to the claimant. It is important to realize that, as far as we can determine, there have not been any instances in which a board of trustees has had a financial judgment made against it.

What we will call trustee liability insurance in this article is akin to directors and officers insurance in a business corporation. Such insurance protects the director or officer against "errors or omissions" in the performance of his or her duties. Trustee liability insurance offers the same type of protection. In a typical policy, the insurance carrier agrees to "pay on behalf of the trustee those sums which the trustee becomes legally obligated to pay as a result of errors or omissions in the performance of his or her duties."

The insurance does not cover every contingency or act. For example, policies may exclude coverage for libel or slander, or activities by which the trustee personally profited, or activities resulting in bodily injury.

Not only is every policy unique, but virtually every institution and its governing board is somewhat different from any other. Consequently, what is appropriate

trustee liability insurance coverage for a large, multi-campus public institution is not necessarily adequate for a small, independent college.

Similarly insurance policies that are available for members of governing boards vary widely. There are currently about 15 insurance companies that offer directors and officers policies to corporations. However, we know of only five which offer trustees and officers policies to colleges and universities—and not even these are written specifically for governing boards. The five are: the CNA Insurance Group, which offers a Board of Education Liability Including School District Reimbursement Policy; the International Surplus Lines Insurance Company, which offers a Directors and Officers Liability and Company Reimbursement Liability Policy; the Insurance Company of North America, which offers a School Professional Legal Liability Insurance Policy; St. Paul Fire and Marine Insurance Company, which offers a Board of Education Policy; and the National Union Fire Insurance Company, which offers a School Leaders Errors and Omissions policy.

The primary feature that makes any of the policies applicable to college and university boards is an endorsement, which simply states that wherever the words "school district" or "school board director" appear, they should be amended to read "college or university" or "board of trustees" or "board of regents."

There are several reasons why there are not a large number of standard policies readily available. Compared to other segments of the insurance market, insurance for trustees is actuarially very small. There is no "typical" governing board. State statutes which allow indemnification of trustees vary, and boards themselves have not always taken advantage of their ability to provide indemnification for their members.

Most important, the environment in which board members have been sued has only been established during the last decade. Similarly, the risks have only recently become understood more clearly with definition and precedent. Consequently, the demand for such coverage has increased dramatically only since that time.

The actual costs of trustee liability policies naturally differ from institution to institution, based on a variety of factors: size and type of institution; the number of trustees; the financial condition of the institution; the limits of liability and the retention (i.e. the amount of deductible). Perhaps surprisingly, a small, private college trustee may in fact need as much coverage as one who serves a large research university with a medical school. It is important to understand that the trustee liability policy is basically a standard policy and that the differences in coverage and cost depend not only on the number and extent of the endorsements to the standard policy (technically known as amendatory endorsements) but, given the above variables, on the underwriter's perception of the potential for liability of the individual trustees with respect to their institution.

Costs

Most insurance companies base their rating (i.e. cost of coverage) on an institution's full-time enrollment (FTE). Some take into consideration the size of the board, the institution's assets and the amount of its revenues. The financial history of the institution, as well, plays a major role in determining its premium. The following examples may help to illustrate the range of costs for such a policy. The rates are based on a three-year, prepaid package and they apply only to the standard policy before any endorsements are added.

A small, private college with less than 1,000 FTE can pay as little as $1,200 for a three-year premium. A medium-

sized college or university with approximately 1,000-3,000 FTE may expect to pay around $1,750, while a large research university may be charged upwards of $100,000. Many institutions purchase policies with a limit of liability of $1 million; smaller institutions may have as little as $500,000 and larger institutions may have as much as $10 million or more. The retention, or deductible, is usually $2,500 but may even go as high as $100,000 again depending on the size of the college or university. As with most insurance, however, the higher the deductible, the lower the premium.

Umbrella Coverage

In addition to the trustee liability insurance provided by the institution for its entire governing board, two other forms of protection are available to individual trustees.

Some corporate directors and officers liability insurance policies may be extended to provide coverage to those members of the corporation's board of directors who also serve as members of not-for-profit governing boards. Such coverage however, is often available only to those who serve not-for-profit boards at the request of the corporation, in effect, serving as the representative of that corporation.

There are two small, but significant, disadvantages to this kind of extended coverage. Foremost, any successful financial claim against a corporate director in his or her position as a college trustee may reduce, for the policy period, the amount of coverage available to other directors of that corporation who also serve as college trustees. Furthermore, when such coverage is extended, an application similar to that for trustee liability insurance may be required. Although neither of these relatively minor problems seem to present insurmountable difficulties, for whatever reason, only a few corporations and insurance companies offer this extended coverage.

More commonly available to individual trustees is the "excess" or "umbrella" policy. Such a policy provides coverage to individuals in excess of required underlying insurance, such as automobile or homeowner's liability insurance. For example, in addition to the standard automobile coverage of $300,000 per accident, and homeowner's liability limits of $100,000 per accident, the individual may purchase additional insurance which subsequently provides limits of liability in excess of the underlying coverage ranging upwards to several million dollars.

Umbrella coverage must be closely examined, preferably with the assistance of a good insurance agent or legal counsel. Its coverage is limited, and activities on not-for-profit boards are often excluded from such policies.

Policy Evaluation

How can you be sure that your institution has purchased the best policy for your needs? We suggest that you consult with both your institution's lawyer and insurance agent and, together, discuss the advantages and disadvantages of at least the five policies mentioned earlier. One policy may include coverage that the others don't, but it may also exclude certain coverages which are particularly appealing—or necessary—to your institution. No one policy will meet every need, but only your board can decide which one best suits your most urgent or likely needs. We also encourage you to use the expertise of the lawyers and insurance people on your board of trustees but, in doing so, to be sure that you avoid any potential conflict of interest in your final decision.

The next sections of this report offer a more extensive and technical discussion of indemnification clauses and actual policies, including such specific terms as severability, discovery of facts which could give rise to a

claim, exclusions, the insuring agreement, and costs and expenses of defense. The analysis has been written by representatives of the insurance industry and lawyers familiar with trustee insurance policies. The examination of specific policy language, applications for insurance coverage and state indemnification statutes will not be for every reader; it is technical and often complex, but we believe it will explain what a lay board member ought to know and understand about trustee liability insurance policies.

SECTION II: Indemnification

Because of the many differences in state laws, methods of operation of institutions and their boards, available insurance policies and types of governing boards, we have concluded that it would be virtually impossible to prescribe or suggest specific protection that would be applicable to all trustees at all institutions of higher education. We do recommend, however, that every governing board examine carefully its own situation before it decides what kind of coverage would best meet its needs. The following section outlines questions which trustees should ask regarding indemnification.

Indemnification Audit

Merely by virtue of their position, trustees are threatened with lawsuits. They can take some comfort, however, in the protection afforded by the statutes which exist in most states allowing indemnification by their institutions of costs, expenses and awards against trustees for their actions. Under such a law, which is usually embodied in the corporation or "not-for-profit" code of the particular state, an institution may indemnify its trustees for claims or actions asserted against them in connection with their positions.

Even though state indemnification statutes exist, there is lack of uniformity among the states as to the protection accorded. Both incumbent and prospective trustees should be certain to acquaint themselves with the protection available in their own jurisdictions. This can be accomplished by asking certain questions and insisting that the answers be used to prescribe the course of action that will subsequently be taken by the institution.

The following questions, phrased in first person singular, will help to elicit information which will be useful in establishing protection for trustees against the risks inherent in their position.

1. In the course of my services and performance as a trustee, I may be subjected to a claim, action, suit or other proceeding. Is there an indemnification statute in my state which allows my institution to protect me against such a claim?

2. If such a statute exists, does the law specify that the institution must indemnify its governing board, or is it discretionary with the institution?

3. If the protection is discretionary, does the indemnification law require some prior or formal act of the governing board of the institution—such as the adoption of a bylaw provision specifying that indemnification *shall* be invoked on behalf of the institution?

4. If such formal action is necessary, has our governing board taken appropriate action to fulfill this requirement so that the protection now applies?

5. Does the protection call for reimbursement to me of expenses that I have incurred or losses that I have suffered, or does it call for payment of such expenses initially and directly by the institution as they arise?

6. Is indemnification provided for threatened matters, or only pending or completed actions?

7. In what situations may I look to the institution for reimbursement or payment? In other words, am I protected in a civil matter? a criminal suit? an administrative charge in which I am involved? an investigative charge?

8. If the situation would otherwise call for reimbursement or payment by the institution, what is the effect of a conviction or a plea of *nolo contendere* by the trustee or officer in a criminal case?

9. Are there any other conditions for seeking such reimbursement or payment from the institution? In other words, is there a requirement of "good faith" or "reasonable belief" on my part in whatever I am charged with having done or having failed to do in order to "qualify" for reimbursement? (Be certain to have the institution's lawyers explain fully all of the ramifications of these or other qualifications.)

10. What items are and are not covered by the indemnification clause—counsel fees? judgments? fines levied against me? amounts paid or owed for settlements reached in order to release me from further action?

Obtaining the answers to the questions posed, and putting into place the appropriate bylaw provisions and procedures to protect trustees, still may not be very reassuring to members of governing boards, given the limited financial resources of many institutions today. Insuring against the risk of ultimate liability and against the rapidly escalating cost of legal defense may be the only realistic means available to protect adequately the institution and its trustees from serious financial consequences.

SECTION III: Policy Coverage

Trustee liability insurance is still a relatively new kind of insurance and the policy forms which provide for it are still evolving. The insurance companies mentioned earlier each offer policies which protect individual trustees, as well as their colleges and universities, from many of the hazards and risks that confront them. And while there are some similarities among the various clauses and areas of coverage, there are also some inherent and obvious differences which are highlighted in the ensuing discussion.

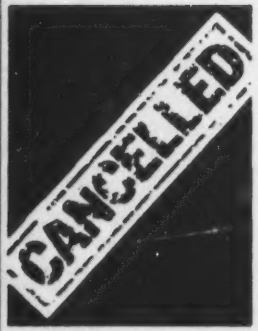
In one case, underwriters for directors and officers liability insurance have modified their policy forms so that they provide some of the protection sought by college and university boards of trustees. Another insurance company which provides coverage for school boards and school districts has similarly altered some of its terms and conditions so that its policies also provide protection for trustees. Still another has modified its school professional policy so that it, too, provides coverage.

Before purchasing such insurance, there are several important areas that a governing board should examine to be sure that it selects the policy that best meets its needs as well as the needs of its college or university. Five of these areas are discussed in more detail in the following section.

Insuring Agreements

Insuring Agreements are those clauses in the policy which define the coverage actually provided by the company to the insured. For trustee liability insurance, each of the policies is drawn to provide coverage on the basis of a claim made against the insured (i.e. the individual trustee, the full board of trustees and/or the college or university) during the policy period. Such coverage is

known as "claims made" insurance. While this is different from automobile and general liability policies, where coverage is determined by the time that the accident or occurrence takes place, it is a typical method of providing coverage for the nature of the liabilities heretofore discussed. It is also characteristic for the insurance to cease at the end of the policy period and, if no claim has been made during the stated time, the insurance thereafter has no further value.



Because it is common with most other insurance policies, many insurance agents or risk managers assume that trustee liability insurance will also provide coverage for acts prior to the date the insurance was written. Some policies, however, are restricted so that they will apply only to claims made during the policy period arising from acts which also occurred during the policy period. Such a limitation is so restrictive, however, that the insurance loses much of its value.

On the other hand, most insurers will cover claims made during the policy period for acts prior to the policy period provided the insured discloses to the insurer in the application for insurance any facts or circumstances which may reasonably be expected to give rise to a claim. Should there be such circumstances, the policy would in the future probably exclude coverage for that particular act.

The information contained in the application then becomes a warranty or representation on which the policy is based. If the information provided is not correct, the insurance carrier could disclaim coverage. For that reason alone, accurate completion of the application is essential.

Insured

In following the general format of directors and officers liability insurance, which provides protection for individual members of the board of directors, it has been recognized that the college or university also should be added as an insured under such a policy. As a result, most policy forms either directly or by endorsement currently include the institution as an insured. In addition, in most instances, it is possible to buy protection on a "broad form" basis, thereby providing coverage not only for the college or university, and its trustees, but also for officers and other specified employees. Thus, at the option of the insured, coverage can be restricted to include only the college or university and its trustees or officers, or it can include a scheduled list of persons other than, or in addition to, the trustees and officers.

Cancellation and Discovery

Because trustee liability insurance is "claims made" insurance, cancellation by the underwriter prior to any claims being made against the board or the institution, immediately exposes them to risk. It also should be noted that the policies are generally cancellable by either party. To avoid the harsh results of such a cancellation by the insurance company, certain protections are built into the policy. Generally a cancellation clause provides for notice to the insured at least 30 days prior to the effective date of cancellation. In the event that cancellation coincides with circumstances which may be expected to give rise to a claim, it is not likely that coverage would be replaced with another carrier. The insured, nevertheless, could still be afforded the protection of the policy if it contains a clause which gives the insured the right to report facts or circumstances which may be expected to give rise to a claim and which furthermore provides that if any claim subsequently arises from those facts or circumstances it will be considered a claim made as of date of notification.

Additional protection is provided in some policies by a "Discovery Clause," which extends coverage of the policy to any claims made during the Discovery period arising out of any "wrongful acts" prior to the termination of the policy. However, if the Discovery Clause is provided at the option of the insurer, not the insured, there is no real protection in the event the insurer cancels. Some policy forms require that the underwriter be given notice of facts or circumstances which may be expected to give rise to a claim, rather than giving the insured an option to report them. Under such forms, the policy becomes much more restricted, since every claim can be questioned on the basis of whether it should have been reported at the time that the act occurred.

Exclusions

As with all insurance, the protection afforded is subject to exclusions which limit the coverage provided. Each of these exclusions should be reviewed to determine whether it eliminates an area of coverage for which the board or institution is seeking insurance. Generally, the scope of exclusions is similar in most policy forms, although the wording may be different. Some, following the directors and officers policy format, separate the exclusions into two categories. One applies to individuals and the other applies to corporate indemnification and to the corporation itself. For the most part, individual exclusions are concerned with personal profit, dishonesty, fraud and return of remuneration which has been improperly received. In some states, insuring against discrimination or other acts against public policy may be excluded from coverage. The other exclusions generally apply to circumstances which are otherwise insured, or to specific categories of hazard which the underwriter for this type of insurance will not accept, such as pollution, the Employee Retirement Income Security Act, and nuclear energy liability.

Applications

In order to assess properly the risks for which insurance is to be purchased, underwriters, before writing the policy, will usually require completion of an application which contains a question designed to reveal facts or circumstances that may reasonably be expected to give rise to a claim. As discussed earlier, the answer to that question becomes a representation or warranty upon which the policy is based. In the event that the answer is not correct, certain legal consequences that could affect the validity of the policy may result.

From the point of view of the insured there are several problems which arise as the policy application is being completed. Since one person (usually someone at the college or university) is answering for several individuals (either board members or officers), he or she may feel it is necessary to question everyone before completing the application. Such a procedure is often difficult, or even impossible. Nevertheless, without further clarification in the policy, serious questions of coverage might arise in the event any one of the individuals had knowledge about facts which could give rise to a claim. Some underwriters have provided that the contents of the application shall be considered severally with respect to each insured and thus have alleviated the problem. If there is no such clause, however, this limitation of the policy should be considered or a procedure for soliciting individual questions devised.

Another potentially more serious problem occurs with renewal, even with the same company, if the insurer requires a new application form. To ask if anyone has knowledge of any facts or circumstances which might

reasonably be expected to give rise to a claim at the time of renewal could effectively cut off continuity of coverage. In other words, if an institution has a policy which has been renewed, the insurance company could disclaim coverage for any claims that are made based on facts or circumstances which occurred during the prior policy period.

This problem is generally resolved by use of a short form renewal application which does not ask for any new warranties or representation about prior knowledge of facts or circumstances. Without the requirement for new representations or warranties, the policy coverage will continue without interruption. When considering which policy to purchase, an institution should consider whether a renewal application form will be available at the end of the policy term, or whether a completely new application form will be necessary which would thereby require a new warranty or representation.

Other Terms and Conditions

Insuring Agreements, Discovery Clauses, definition of Insured, Exclusions and the Application are just a few of the areas which should be investigated when considering purchase of insurance of this nature. Others include such provisions as control of the defense for the suit, or choice of the lawyer(s) to defend the trustees and the institution if a claim is in fact made. A close review of the policy terms and conditions should be undertaken with a knowledgeable insurance broker and the institution's lawyer and/or risk manager.

Trustees should remember, however, that trustee liability insurance does not insure against every risk. For example, it does not protect the criminal, nor the self-dealer who attains personal gain or enrichment, nor the dishonest person. And it does not ordinarily provide protection against intentional or willful acts such as libel, slander or assault. On the other hand, legal expenses and monetary judgments arising from challenges to matters of management, whether defended successfully or not, would most likely be covered by a typical indemnity policy. Regardless, monetary settlement of such suits, either directly by the insurance carrier or subject to its approval, is authorized under many such policies. Such a provision might make possible a more expeditious and practical disposition of a lawsuit than would a protracted court case.

Conclusion

No degree of caution can guarantee that an institution will not be sued by those who believe they have been wronged. Increasingly, therefore, trustees need to be aware that there are certain actions that they can take to reduce substantially their exposure to liability. These include assessing closely and continuously their legal and fiduciary responsibilities; adopting the procedures outlined in this paper, and subsequently asking for a periodic study of their risks for personal liability; and finally, consulting with their institution's risk manager, insurance broker and lawyer to be sure that they purchase a trustee liability policy which best meets their needs as well as the needs of their institutions.

For additional information on related publications, sample policies, and clarification on any of the issues raised in this report, readers are encouraged to contact the Trustee Information Center at the Association of Governing Boards of Universities and Colleges, Suite 400, One Dupont Circle, Washington, D.C. 20036 202/296-8400.

Illustrative Risks

Illustrative Risks Covered By General Liability Insurance or Trustee Liability Insurance

Covered by general liability policies

Student accidents while on college business
Medical school (hospital) problems
Athletic injuries
Campus security
Physical plant
Student public defamation
Invasion of privacy
Failure to supervise student housing
Assault and battery
False arrest

Covered by directors and officers or school board policies

Tenure
Accreditation
Faculty appointment/dismissal
EEO charges
Sexual harassment
Investment of endowment
Student discipline/expulsion
Conflict of interest
Bankruptcy
Mismanagement of institutional finances
Misuse of financial aid funds
Breach of fiduciary responsibilities in closing the college
Student admissions procedures/requirements
Collective bargaining
Violations of contract (can sometimes be covered by general liability)
Faculty personnel policies
Incompetent teaching
Breach of duty of loyalty
Failure to exercise ordinary and reasonable care in the performance of duties
Violation of constitutional rights of students and faculty
Violation of due process
Failure to follow correct procedure for maintaining tax-exempt status

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